

GVNW Consulting, Inc.
Comments in WC Docket Nos. 05-195, 02-60, and 03-109; CC Docket Nos. 96-45, 02-6, and 97-21
October 18, 2005

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Comprehensive Review of Universal)	WC Docket No. 05-195
Service Fund Management,)	
Administration, and Oversight)	
)	
Federal-State Joint Board on)	
Universal Service)	CC Docket No. 96-45
)	
Schools and Libraries Universal Service)	
Support Mechanism)	CC Docket No. 02-6
)	
Rural Health Care Support Mechanism)	
)	WC Docket No. 02-60
Lifeline and Link-Up)	
)	WC Docket No. 03-109
Changes to the Board of Directors for)	
the)	CC Docket No. 97-21
National Exchange Carrier Association,		
Inc.		

COMMENTS OF GVNW CONSULTING, INC.

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Executive Summary

While the Commission attempts to provide USAC with oral and written guidance as well as regulation through its rulemaking process, delays in the Commission's response to direct questions regarding the correct interpretation of these rules tends to put a cloud of uncertainty over the process for impacted carriers.

There is not a need for radical change that would serve to sweep away the many good aspects of current USF administration. While the universal service support mechanisms are the subject of current scrutiny and criticism, there is no evidence of pervasive waste, fraud, and abuse. The Commission must keep in mind that rural infrastructure costs are not paid in full up

front, as the cost of maintaining and upgrading facilities is an ongoing process. Universal service support mechanisms have played a key role in assuring that rural customers have been able to receive affordable service.

As the Commission reviews the current USF administration process and contemplates refinements, an important metric to keep in mind is that the administrator must possess a thorough knowledge and understanding of the telecommunications industry, especially the circumstances facing rural ILECs that provide service in high-cost areas.

The Commission should also take steps to assure that USF programs are administered in an equitable manner, responsive to the needs of all participants, and receptive to input from diverse constituencies.

One specific area that merits review is the requirement to certify forecasts and projections. We recommend the Commission consider modifying the rules to require carriers to state that they have completed a good faith effort and used reasonable judgment with regard to estimates and projections. Many rural ILECs experience greater variances in expenses and investment than larger carriers, and this should be reflected in any revised rules.

While we believe it unlikely that the Commission will exempt any carrier based on its small size, the Commission should exercise prudence with respect to the burden placed on the smallest carriers with regard to audit burdens. It would be patently unfair if the audit sample contained a large number of smaller carriers just because it would be easier to audit a smaller carrier. The Commission should consider both a screening mechanism and risk identification process to focus a potential review, and selecting an audit sample that provides a statistically significant degree of confidence (e.g., 95%) that the audit goals have been achieved. The Commission should ensure that any audit program passes a fundamental cost vs. benefit analysis, as the record does not indicate that there is pervasive waste, fraud, and abuse occurring among high-cost support recipients.

We recommend that any “normal” audit or investigation be limited to a twelve month period after the audit or investigation has commenced. In the event that the investigation discovers fraudulent activity, a procedure could be available that would provide for a waiver of the twelve month cycle and grant an extension of time for the review.

INTRODUCTION AND BACKGROUND

GVNW Consulting, Inc. (GVNW) is a management consulting firm that provides a wide variety of consulting services, including regulatory and advocacy support on issues such as universal service, advanced services, and

access charge reform for communications carriers in rural America. The purpose of these comments is to respond to the Notice of Proposed Rulemaking (NRPM) and Further Notice of Proposed Rulemaking (FNPRM) released by the Commission on June 14, 2005.

We have participated actively in prior rulemaking proceedings and applaud the Commission's current efforts to address the myriad of challenges facing universal service programs today. As we will demonstrate in this comment filing, there is not a need for radical change that would serve to sweep away the many good aspects of current USF administration. While the universal service support mechanisms are the subject of current scrutiny and criticism, there is no evidence of pervasive waste, fraud, and abuse. The Commission must keep in mind that rural infrastructure costs are not paid in full up front, as the cost of maintaining and upgrading facilities is an ongoing process. Universal service support mechanisms have played a key role in assuring that rural customers have been able to receive affordable service as promised under TA 96¹.

¹ An observation from Theodore Vail, AT&T's President from 1907-1920 assists in demonstrating that universal service predates the last ten years of struggle with TA 96: "there should also be state protection – protection to a corporation striving to serve the whole community. . . from aggressive competition which covers only that part which is profitable." Statement of Bell Chairman Theodore Vail, quoted from G. Brock, *The Telecommunications Industry: The Dynamics of Market Structure*, page 159 (1981).

We respectfully submit these comments for the Commission's consideration, and have organized our comments to mirror the structure and organization of the Notice and Further Notice.

MANAGEMENT AND ADMINISTRATION OF THE USF

At paragraph 4, the Commission indicates that "USAC administers the USF in accordance with the Commission's rules and orders." This paragraph also indicates that "The Commission provides USAC with oral and written guidance as well as regulation through its rulemaking process." The effectiveness of this stated process of providing guidance merits a careful review for reasons stated below. The process may also lead to speculation that the Commission's "oral" guidance may not be consistent with the written rules. Delays in the Commission's response to direct questions regarding the correct interpretation of these rules tend to put a cloud of uncertainty over the process for impacted carriers. We provide the following examples:

- From the inception of the HCL Universal Support mechanism there has been a lag between the data period used for calculating the Universal Support and the Expense adjustment period. This is codified in the rules in Sub part F of Part 36. (See Part 36.601(b), 36.611 and 36.612). When the Commission adopted the Safety-valve procedure it indicates these same rules should be used for calculating the index period expense adjustment. USAC, however,

is administering the safety-valve as if the index period were the data period resulting in a permanent shifting of the support out about two years and significantly changing the index period calculated expense adjustment. Attempts to address this issue with USAC fell on deaf ears for several years. On January 13, 2005 we brought this issue to the Commission for clarification. The Commission's lack of response to this matter brings into question whether USAC was orally told to administer the safety-valve inconsistent with the Commission's written rules. Another concern is that the Commission intended the process to be administered differently than the rule, but it did not change the rule to be consistent with what is intended nor does the Commission provide any response to specific requests to guide the companies that are subject to these rules.

- Another example relates to the administration of the Local Switching Support (LSS) mechanism. USAC is attempting to administer the limitation in Part 54.301(a)(3) as if Part 36.125(a)(5) specified the use of the 1996 unweighted DEM factor. The rule does not specify this, and this rule has been administered by NECA for years applying the rule as written. It is unclear if USAC is doing this because of "oral" instructions from the Commission, or if they

choose to do this on their own rather than seeking authorization to collect the information to do the calculation as per the rules. This issue has been referred to the Commission in a June 20, 2005 appeal from North-State Telephone Company. (Confirmation #2005620002125). Please note that Part 54.724 requires that the Commission take action within 90 days of the appeal. As of the date of this filing, we have received no response from the Commission.

We respectfully submit that there needs to be some attention paid to resolving questions and issues related to the administration of the Universal Service Funds. This can be handled through the Commission assigning adequate resources to the task, or through a process of issues resolution similar to NECA's process used for the Access Pooling process. Using NECA's process, a large number of the issues could be addressed and possibly resolved with limited input from the Commission with only the more controversial issues being formally presented to the Commission for resolution.

The current process is frustrating as the Commission is not responsive to requests for clarification and guidance. A couple more examples are as follows:

- On June 16, 1998 GVNW requested interpretation of several provisions in the Commission's Rules Parts 32, 36, 54, and 69. To date, the Commission has not provided a response to these questions. On March 6, 2002 we refreshed the record with regards to these questions again requesting that the Commission address the pertinent questions.
- On January 23, 2004 GVNW requested interpretation and guidance regarding several tax issues that impact the pooling process and the Universal Service Support. The Commission has not yet responded with the needed guidance in interpreting the related rules. This item is further exacerbated by NECA's decision to override the companies balance of plant related deferred taxes which we are allocating per Part 36.506. NECA is picking out sub-account amounts that may have a debit balance and adjusting these sub-accounts to a zero balance which results in an inflated balance of plant related deferrals in the cost study.

Additional evidence for the record regarding the question of whether the USAC is administering the support funds according to the rules is found by examining another apparent departure from the rules by USAC. This departure relates to the treatment of AFUDC in the LSS computation. There are two different issues associated with the treatment of AFUDC as follows:

- Allowance for Funds Used During Construction (AFUDC) is an income item, not an expense. USAC is including the AFUDC as if it were an expense included in Part 54.301(d)(3). The rules make no mention of using this income item as a direct component of the LSS requirement, rather it is listed as a tax component in Part 54.301(d)(4).
- We also question the Commission's intent with regards to the inclusion of AFUDC in the tax computation. We believe it would be appropriate to include the AFUDC in the tax computation if the AFUDC was not includable on the tax return. Under current tax law, however, AFUDC is includable in taxable income. It is possible that the rate for computing AFUDC is different for tax purposes and for book purposes, and if this is the case, the amount of the AFUDC which shows up on the Schedule M-1 of the tax return should be included in the LSS tax computation. It appears from the wording in the rule that the Commission is asking for the full AFUDC rather than the M-1 amount.

In a recent audit review, USAC has initially denied a subchapter S company tax recovery indicating that it was not allowed for Universal Service Support computations. USAC, however, did not provide any authoritative support for this position which seems contrary to court decisions and other regulatory bodies' treatment of taxes on "pass through" entities. (See FERC

Policy Statement on Income Tax Allowances May 4, 2005. 111 F.E.R.C.

P61,139 Docket No. PL05-5-000).

Universal Service Fund Administrator

As the Commission reviews the current USF administration process and contemplates refinements, an important metric to keep in mind is that the administrator must possess a thorough knowledge and understanding of the telecommunications industry, especially the circumstances facing rural ILECs that provide service in high-cost areas. One approach that would facilitate this objective would be the use of long-term contracts² or appointments for the administrative entity to ensure adequate institutional knowledge and understanding of the telecommunications industry.

The Commission should also take steps to assure that USF programs are administered in an equitable manner, responsive to the needs of all participants, and receptive to input from diverse constituencies.

The administrative entity must also be able to work cooperatively with other designated entities. In accordance with current Commission rules, the NECA plays an important role in administering access charges. In light of the interrelationship between universal service funding and access charges,

² While the Commission will likely receive comment that a competitive bidding process would provide some economic benefit, the Commission should also assess the administrative burden inherent in such a process for both recipients and contributors with the likely change in forms and procedures that would follow from a change in administrative entity.

the Commission should encourage the USF administrator to work closely and cooperatively with the NECA to ensure that the settlement process is smooth and seamless. There is a benefit to the dual role that NECA plays with regard to providing the cost data, and USAC handling the administrative portion of the USF programs.

Performance Measures

At paragraph 30, the Commission seeks comment on adopting meaningful outcome, output, and efficiency measures for the High Cost, Rural Health Care, and Low Income programs.³ Because these mechanisms have different goals and purposes than the E-rate program, the Commission states that it expects to adopt different performance measures and goals for each program. We support the adoption of individual performance measures for each of the separate mechanisms.

Application Process

The Commission seeks proposals from stakeholders on ways to improve the High Cost program application process and participation by reducing or eliminating the administrative burden on carriers. Comments also should discuss whether the Commission should permit High Cost carriers to file annual, biannual, or triennial applications for support to

³ These programs are codified in Part 54 of the Commission's rules. The High Cost program is in Subpart D, the Low Income program is in Subpart E, the Schools and Libraries program is in Subpart F, and the Rural Health Care program is in Subpart G.

provide for a more efficient administration of the High Cost program while minimizing the burden on carriers.

Beginning at paragraph 44, the Commission asks how the application and administrative process can be improved for participating in the High-Cost program and whether the timing and content of reporting requirements need to be modified.

One specific area that merits review is the requirement to certify forecasts and projections. We recommend the Commission consider modifying the rules to require carriers to state that they have completed a good faith effort and used reasonable judgment with regard to estimates and projections. Many rural ILECs experience greater variances in expenses and investment than larger carriers, and this should be reflected in any revised rules.

While the Commission may not choose to change the existing procedures, it does not appear to be competitively neutral for ILEC support to appear on the USAC website on a study area basis for each type of support received while CETC data is provided on a statewide basis.

We support the continuation of the existing structure of mandatory annual filings, with carriers having the option of providing quarterly updates of high-cost data. Mandating a quarterly filing cycle would impose unnecessary administrative costs on many rural carriers.

At paragraph 50, the Commission poses the question as to whether section 54.301 should be revised to limit projected growth in accounts based on actual past performance. Due to the unique cost characteristics of rural carriers, the Commission must exercise caution if it attempts to develop rules related to forecasted cost data. For some small carriers, significant switching upgrades will not occur each and every year, but instead will happen in year 200x and then not again until year 200x+5. If rules were in place that limited a rural ILECs data forecast change to some fixed percentage, rural carriers would be penalized for their unique operating circumstances.

USF Disbursements

At paragraph 61, the Commission asks whether the existing disbursement process for the High-Cost program should be revised, including the concept of a single uniform system. We do not support such a change, as a single uniform disbursement process would result in unnecessary detail and would likely be confusing to both participants and contributors. Given the different separations rules for the high-cost loop fund, LSS, and ICLS programs, a change in the current disbursement process could produce a negative impact on a carrier's cash flow. It is important to keep in mind that carriers already have to wait two years to receive reimbursement for funds expended under the high cost loop program.

OVERSIGHT OF THE USF

Independent Audits

Beginning at paragraph 69, the Commission asks whether the current audit structure for the High-Cost program is appropriate and whether the FCC's rules should require independent audits of fund recipients.

We submit that any proposed audit plans should be targeted and focused to high risk areas, and recognize that rural ILECs are already being reviewed and audited by independent external auditors, various other agencies, and the NECA.

Many companies have an annual audit of their corporate financial statements. In the course of these audits, the independent audit firm performs tests of internal controls. All independent audit firms are subject to AICPA rules and have recently increased audit requirements related to fraud issues in this post-Enron environment.

The NECA also reviews company financial data for consistency between the company records, cost study data, and USF data. This NECA review includes steps that provide assurance that all financial data reconciles to the company's financial statements and the balances that are subject to separations (post Part 64).

While we believe it unlikely that the Commission will exempt any carrier based on its small size, the Commission should exercise prudence with

respect to the burden placed on the smallest carriers with regard to audit burdens. It would be patently unfair if the audit sample contained a large number of smaller carriers just because it would be easier to audit a smaller carrier. The Commission should consider both a screening mechanism and risk identification process to focus a potential review, and selecting an audit sample that provides a statistically significant degree of confidence (e.g., 95%) that the audit goals have been achieved. The Commission should ensure that any audit program passes a fundamental cost vs. benefit analysis, as the record does not indicate that there is pervasive waste, fraud, and abuse occurring among high-cost support recipients.

Any carrier audited should be allowed to treat the audit preparation and audit performance as interstate expenses recoverable from that jurisdiction.

We also support the concept of auditing fund contributors. At paragraph 80, the Commission notes that a threshold of \$100 million would result in approximately 60 percent of the contribution base receiving potential attention.

Documentation Retention Requirements

At paragraph 83, the Commission asks about document retention requirements for High-Cost Fund recipients. We recommend that fund

recipients should be required to retain documents in accordance with normal business practices (e.g., seven years for tax purposes).

Administrative Limitation Period

Beginning at paragraph.86, the Commission seeks comment on the establishment of an administrative limitations period for audits or other investigations of High-Cost fund recipients. We support such a limitation, and recommend that any “normal” audit or investigation be limited to a twelve month period after the audit or investigation has commenced. In the event that the investigation discovers fraudulent activity, a procedure could be available that would provide for a waiver of the twelve month cycle and grant an extension of time for the review.

Measures to Deter Waste, Fraud, and Abuse

In view of the Commission’s concerns with respect to waste, fraud, and abuse, the Commission should retain current NECA review processes, as this form of validation enhances the credibility of the programs. At paragraph 92, the Commission seeks comment on measures the FCC can take to prevent waste, fraud and abuse in the High-Cost program. If intentional waste, fraud, or abuses are uncovered, the Commission currently possesses the ability to levy fines and sanctions.

It is also crucial for the rules to distinguish between ministerial error and errors that are the result of intentional fraud or negligence. With the

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amount of data that is input related to support mechanisms, there will be an occasional input type error. In terms of penalties, there should be clear distinction between ministerial error and errors based on intent to deceive.

Other actions

At paragraph 97, the Commission asks whether the FCC should adopt debarment rules applicable to the High-Cost program. If intentional waste, fraud, or abuses are uncovered, the Commission currently possesses the ability to pursue debarment.

Respectfully submitted

Via ECFS on 10/18/05

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